Three Ways to Access Money from Your Home

By Robert E. Whitney, Jr., CFP®, Senior Financial Planner

Do you have a major expense coming up in the near future? If you don't have the cash on hand to cover it – or would rather consider other ways of paying for it – tapping into the equity in your house might be a good option. You can do this in one of three ways: a home equity loan, a home equity line of credit (HELOC), or a cash out refinance.

Secured by your home, each of these options has the benefit of offering lower interest rates and higher borrowing limits than personal loans. The interest you pay may also be tax deductible; however, you should always consult with your tax professional to make sure this is the case in your situation. Bottom line, all three options could save you money when compared to other financing choices.

Whatever you need the money for – a wedding, college costs, home improvements, medical expenses, debt consolidation – the equity in your home may provide the perfect solution. In fact, using a home equity loan, HELOC, or cash out refinance can be a smart way to get the funds you need. The applicable interest rates are typically lower than conventional loans or borrowing through credit cards.

Here's how each of the three options could be a viable solution for your funding needs.

Homeowner Equity Value Has More Than Doubled in Recent Years

The value of homeowner equity in the U.S. has been on the increase during the past decade. Since 2010, homeowner equity has grown from approximately $8.77 trillion to approximately $21.1 trillion in 2020.

To calculate home equity value, subtract the value of remaining mortgage debt from the market value of the real estate property. The value of home equity increases as the debtor pays off the mortgage.[1]

Home Equity Loan

Home equity loans are a smart choice if you have a single large expense, know exactly how much money you'll need, and like knowing what your payment will be each month. Here are a few benefits with this option:

- The loan amount is provided to you all at once.
- These loans have a fixed rate and fixed monthly payments, so it's easier to budget.
- The term and repayment options are flexible, so you can choose the ones that best fit your needs.
- With many lenders, this type of loan has no closing costs, origination fees, or early payoff fees.

For example, let's say your home is valued at $500,000 and you have 20 years remaining on a 30-year mortgage with an outstanding balance of $200,000. This type of loan does not change your original mortgage. Your home is your collateral and, depending on the lender, you can generally borrow 70% to 90% of your home's value. You could qualify for a loan up to $150,000 in addition to the $200,000 outstanding mortgage for a total of $350,000 (70% of $500,000). If the loan is used to buy, build, or substantially improve the home from which you are borrowing, it's potentially tax deductible.

Home Equity Line of Credit (HELOC)

If you need funds to cover expenses incurred over a longer period of time and you're comfortable with variable interest rates, a HELOC offers the flexibility and convenience of ongoing credit. HELOCs are well suited for longer term expenses or if you aren't sure how much cash you'll need or when you'll need it. This is also a good option for an emergency – funds can be accessed quickly and easily.

Here are a few reasons why a HELOC might be a good choice for you:

- You can access the funds as soon as you close and continue to use them for the life of the line of credit, up to the approved limit.
- Your payments and interest are based only on the funds you actually use, and they may be as low as interest only. Any remaining balance is due in a "balloon" payment at the end of the loan term.
- HELOCs offer a variable interest rate that follows the market and could potentially have a lower rate than other lending options.
- Depending on the lender, HELOCs often allow you to access your funds in multiple ways, e.g., write a check, transfer funds online, or visit a branch location. And many HELOCs have no closing costs, origination fees, or early payoff fees.

Going back to our example of a home valued at $500,000 with $200,000 remaining on the mortgage, you could qualify for a revolving credit line of $150,000. You could borrow $25,000 now for a new bathroom, and $75,000 later for a new kitchen – leaving $50,000 for future improvements. Again, if the money is used to buy, build, or substantially improve your home, the funds are potentially deductible.

Cash Out Refinance

With the third option of a cash out refinance, let's say you've paid down the balance of your original $200,000 mortgage in the example above to $150,000. You could refinance at current interest rates for the original mortgage amount maintaining a similar monthly payment and take the difference ($50,000) to use however you'd like by extending the term of your mortgage. Typically, this is done at a fixed rate (usually lower than a home equity loan or HELOC) because you are just increasing your mortgage. Mortgage interest is tax deductible up to $750,000. However, this option can be more expensive because of mortgage closing costs.

We Can Help

If you want to make your dreams a reality, the financial power that comes with accessing the equity in your home is a great place to start. Contact Commerce Trust Company today – we're here to answer all your questions and help you determine which borrowing option is appropriate for your financial situation.

[1] Statista Research Department, “Volume of homeowner equity in the U.S. 1960-2020,” https://www.statista.com/statistics/375865/value-of-homeowner-equity-usa/, April 20, 2021.

General Resource: Commerce Bank, “Home equity loan vs. a home equity line of credit: what’s the difference?”, January 31, 2020.

The opinions and other information in the commentary are provided as of December 14, 2021. This summary is intended to provide general information only, and may be of value to the reader and audience.

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Robert E. Whitney, Jr., MBA, CFP®

Vice President, Senior Financial Planner

Rob is a senior financial planner for Commerce Trust Company. He is a member of the financial advisory services team — a dedicated financial planning practice within Commerce Trust that provides objective financial advice to clients. Following a thorough assessment of a client's unique situation and thoughts regarding wealth, Rob develops holistic and coordinated plans to help clients meet their short-term and long-term goals as well as take full advantage of various planning, tax, and investment strategies along the way. With more than 16 years of experience, he specializes in building relationships with clients and providing comprehensive financial planning services to business owners and individual investors to help them achieve their goals. Rob holds the CERTIFIED FINANCIAL PLANNER™ designation. He received his bachelor of administration degree in business finance from Loyola University in Maryland and his master of business administration degree from the University of Delaware. Rob serves on the Allocation Panel for the United Way of Greater St. Louis. Additionally, he is an Eagle Scout.

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